

# SUMMARY ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Wyman Analyst: Marion Mann DeJong Bill Number: AB 2304

Related Bills: See Prior Analysis Telephone: 845-6979 Amended Date: 04/30/2002

Attorney: Patrick Kusiak Sponsor: \_\_\_\_\_

**SUBJECT:** Employer Credit for Wages Paid to Employees for Aviation Property

DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced/amended \_\_\_\_\_.

AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.

☒ AMENDMENTS DID NOT RESOLVE THE DEPARTMENT'S CONCERNS stated in the previous analysis of bill as introduced February 21, 2002.

☒ FURTHER AMENDMENTS NECESSARY.

DEPARTMENT POSITION CHANGED TO \_\_\_\_\_.

☒ REMAINDER OF PREVIOUS ANALYSIS OF BILL AS INTRODUCED February 21, 2002, STILL APPLIES.

OTHER - See comments below.

## SUMMARY

This bill would create a credit for wages paid by an employer for work performed on items installed in aircraft.

## SUMMARY OF AMENDMENT

The April 30, 2002, amendments would make the following changes.

- Clarify what contracts qualify for the credit.
- Clarify the definition of qualified employee.
- Add definitions for "manufacture," "property for use in aircraft," and "research."
- Extend the credit carryover period from eight to 14 years.
- Specify that a taxpayer cannot claim both this credit and the Joint Strike Fighter (JSF) wage credit.

The amendments resolved some implementation and policy considerations, and partially resolved other considerations discussed in the department's analysis of the bill as introduced February 21, 2002. In addition, the amendments raised an additional policy consideration. The "This Bill," "Implementation Considerations," and "Arguments/Policy Concerns" discussions from the department's prior analysis have been revised to reflect the amendments and are provided below. The "Legal Impact" discussion is reiterated below for convenience. The remainder of the department's prior analysis still applies. The Board position remains pending.

Board Position:

<input type="checkbox"/> S	<input type="checkbox"/> NA	<input type="checkbox"/> NP
<input type="checkbox"/> SA	<input type="checkbox"/> O	<input type="checkbox"/> NAR
<input type="checkbox"/> N	<input type="checkbox"/> OUA	<input checked="" type="checkbox"/> PENDING

Legislative Director

Date

Brian Putler

5/10/02

## Summary of Suggested Amendments

Amendments are needed to resolve the implementation concerns discussed in this analysis. Department staff will be available to assist the author with amendments as the bill moves through the legislative process.

## ANALYSIS

### THIS BILL

This bill would create a wage credit, similar to the JSF wage credit, for taxpayers located in California that are under a contract or subcontract with the U.S. Department of Defense (DOD), any branch of the U.S. military, the National Aeronautics and Space Administration (NASA), or a private commercial or general aviation company to research (as defined), develop, manufacture (as defined), test, distribute, or refurbish property that is physically installed in aircraft. The contract must be executed on or after January 1, 2003, and before January 1, 2013 to qualify for the credit.

The credit would be equal to a percentage of wages paid to employees as follows:

<b>Taxable Years</b>	<b>% of wages</b>
Beginning on or after January 1, 2003, and before January 1, 2005	50%
Beginning on or after January 1, 2005, and before January 1, 2007	40%
Beginning on or after January 1, 2007, and before January 1, 2009	30%
Beginning on or after January 1, 2009, and before January 1, 2011	20%
Beginning on or after January 1, 2011, and before January 1, 2013	10%

Only the portion of wages that are direct costs, as defined in Section 263A of the Internal Revenue Code, and are allocable to property that is researched, developed, manufactured, tested, distributed, or refurbished for use in aircraft pursuant to a contract or subcontract with one of the entities listed above would qualify for the credit.

The wages could be paid to new or existing employees, 90% of whose services are performed in California for the taxpayer and whose services are directly related to the taxpayer's contract or subcontract for aircraft property. The credit would be limited to \$10,000 per year, per employee, and be prorated for partial years.

Any credit in excess of tax liability could be carried forward for up to 14 years. No credit would be allowed unless the bid upon which the contract or subcontract is based is reduced by the credit amount. The taxpayer would be required to provide, at the request of the Franchise Tax Board, all references to the credit and ultimate cost reductions incorporated into any successful bid that was awarded a contract or subcontract.

Taxpayers that claim this credit cannot claim the JSF wage credit if they claim this credit, regardless of whether the wages qualify for both credits.

### IMPLEMENTATION CONSIDERATIONS

This bill would raise the following implementation concerns. Department staff is available to assist the author with amendments as the bill moves through the legislative process.

- The term “private commercial or general aviation company” is unclear. Does this mean a “private commercial company” (i.e., any business) or, does it mean a “private commercial aviation company and a general aviation company?” The bill should specify whether the contractor must be an “aviation” contractor to qualify. Also, the terminology is very broad and may bring in unexpected taxpayers such as flight schools or charter flight companies that “refurbish” their aircrafts. Contracts entered into with these companies can be substantially different than those entered into with the remainder of the referenced group such as the DOD, military, and NASA.
- The terms “develop,” “test,” “distribute,” or “refurbish” are not defined. Undefined terms can lead to disputes between taxpayers and the department.
- “Aircraft” as used in this bill appears to be broad in nature, covering simple aircraft such as twin-engine craft to aircraft such as commercial passenger airliners, military aircraft, and spacecraft. The author may want to specifically define the group of aircraft intended for the credit.
- The requirement that the credit be reflected in the bid will likely lead to disputes between taxpayers and the department because if a bid is reduced and the credit cannot be used (expires during the carryover period), then taxpayers cannot recoup the money. Further, this requirement may be a compliance issue given the large number of potential contracts and subcontracts. However, the amendment to extend the carryover period from eight to 14 years may reduce the impact of this concern.

### **LEGAL IMPACT**

This bill would define “qualified taxpayer” as a taxpayer “in this state” under a contract or subcontract for aircraft property. A requirement that a taxpayer be located in California may be subject to constitutional challenge under the Commerce Clause of the United States Constitution. Simply removing the requirement from the definition of “qualified taxpayer” and letting the “qualified employee” definition provide the rule that the work must be performed in California would likely avoid this challenge.

### **ARGUMENTS/POLICY CONCERNS**

This bill would allow taxpayers to claim multiple credits for the same expenditure since it does not contain a provision restricting the taxpayer to one credit based upon wages paid to a single employee. Currently, the enterprise zone hiring credit and the research credit are available for wage expenditures covered under this bill for some or all taxpayers.

Although the bill was amended to prevent taxpayers from claiming both this credit and the JSF wage credit, the amendment did not restrict the limitation to credits for the same expenditure. Thus, if the taxpayer pays wages to one employee for work done on aircraft other than a JSF, and pays wages to another employee for work done on a JSF, the taxpayer would have to choose one credit.

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